

DOCKET FILE COPY ORIGINAL

FILED/ACCEPTED
OCT 31 2006

Federal Communications Commission
Office of the Secretary

BEFORE THE FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of the Federal-State Joint)	WC Docket No. 05-337
Board on Universal Service Seeking)	
Comment on the Merits of Using Auctions)	CC Docket No. 96-45
To Determine High-Cost Universal)	
Service Support.)	

Initial Comments
of
Montana Independent Telecommunications Systems

October 10, 2006

Michael C. Strand, General Counsel
P.O. Box 5237
Helena, MT 59604-5237

043
MARCODE

I. Introduction

These comments are submitted pursuant to the request for comments released August 11, 2006, by the Federal-State Joint Board on Universal Service (Joint Board) regarding the merits of using reverse auctions to determine high-cost universal service support. Specifically, the Joint Board asks for comment regarding whether and how “reverse auctions” could be utilized to further goals of the Federal Telecommunications Act of 1996 (Act) and the Commission’s universal service goals.

Montana Independent Telecommunications Systems (MITS) is an organization of rural telecommunications companies headquartered across Montana and serving some of the most remote, sparsely populated, and high-cost areas of the United States.¹ All MITS’ members receive high-cost support for their landline operations, and all MITS’ members provide broadband services to between 90% and 100% of their subscribers, depending on the particular circumstances of the member. One of MITS’ members also receives high-cost support for its wireless operations, and another of MITS’ members is currently seeking high-cost support for its wireless operations.

As noted in the Joint Board’s Public Notice, this issue has been released for comment in the past and MITS filed comments at that time.

¹ MITS members are: Central Montana Communications, InterBel Telephone Cooperative, Nemont Telephone Cooperative, Northern Telephone Cooperative, Project Telephone Company, Southern Telephone Company, and Triangle Telephone Cooperative Association.

From our perspective, little has changed with respect to pros and cons of reverse auctions as a method of distributing high-cost support. As was the case two years ago, the nature of the specific rules and regulations surrounding the reverse auction distribution mechanism is of primary importance. In the absence of adequate regulatory safeguards, reverse auctions are noteworthy mainly (and perhaps solely) because they tend to drive the financial demands on the high-cost fund downward. For some, this quality alone would be sufficient justification for using reverse auctions. None of the universal service principles set forth in the Act, however, states that the high-cost portion of the Fund should be as small as possible.

However, we would be not only remiss but naïve if we failed to recognize that the greatest change in the area of universal service over the past several years has been the growth in demand for high-cost funding. As more and more entities seek and are granted ETC designation, the Fund continues to grow, particularly given the continued existence of the identical support rule. As the fund grows, so does the political pressure to somehow contain that growth. In an era of mushrooming federal deficits, this is understandable.

Admittedly, reverse auctions *may* be a way to slow or reverse the growth in the high-cost fund. However, the fact is that there are a great number of ways to slow or reverse that growth, including funding caps, limits in the number of ETCs that can be designated in a particular market,

redefining eligibility requirements for funding, etc. Unfortunately, the *problem that is common to most of these methods, including reverse auctions*, is that they focus primarily or even exclusively on controlling growth at the expense of the substantive universal service policies that are intended to benefit rural and inner city America. Again, the critical issue is, therefore, the safeguards set forth in the rules and regulations surrounding any given strategy for containing growth. The Joint Board clearly recognizes this since it has provided an example of a set of rules and regulations that could govern a reverse auction methodology in the "Discussion Proposal" attached to its Public Notice in this proceeding.

II. Issue: Whether there are conditions under which auctions for universal service support yield significant benefits to the preservation and advancement of the fund.

This is one of the first issues listed in the Public Notice on which the Joint Board seeks comment. As worded, the answer to the issue is yes, such auctions can yield benefits to the preservation and advancement of the fund. If high-cost support is awarded to the provider that indicates it can provide service for the lowest amount of support, of course such an approach will minimize the size of the fund. Presumably, the smaller the fund the easier it will be from a political standpoint to preserve.

However, if the issue were worded slightly differently, so that instead of the word "fund," we inserted the words "universal service," the issue becomes

much more difficult. Providing funding to the lowest bidder does not so clearly preserve and advance “universal service.” The motivation of the bidder is to devise a business plan that allows it to provide (as the Public Notice describes it) “an acceptable quality of service for a specified term” at the lowest possible cost so that it can win the bid and yet generate an acceptable return to its investors. At least in the minds of MITS’ members, the possibility of all of the successful bidders across the country actually being successful in this endeavor would be a miraculous coincidence. It stands to reason that some number of bidders across the country will, during the bidding process, be unduly aggressive in their bids and wind up underestimating the costs of providing “an acceptable quality of service.” What happens to the principles of universal service in such cases? We presume that they are not going to be allowed to go to USAC and say, “Oops! We can’t provide an acceptable level of service with the amount of support you have awarded us so please award us more.”

Instead, such providers are either going to have to raise their prices so that they can provide “an acceptable quality of service,” or they are simply going to have to provide a quality of service that is unacceptable. Either way, we would submit that such providers would neither be preserving nor advancing the substantive goals of universal service, such as ensuring that

services in rural areas would be reasonably comparable in quality and price to those available in urban areas.²

Again, every bidder across the country could, by miraculous coincidence, make their bid and implement the service at that level of support with absolute success. But assuming some don't, the news gets even worse. Telecommunications (at least for those who provide their own facilities) is a capital-intensive business. Hardware and software has to be changed out on a timely basis and technology changes fairly rapidly. In a sparsely populated rural area, if a newcomer with a technology that has not been fully proven is the successful bidder but is unable to actually offer an acceptable quality of service during the ten-year period for which it is the winning bidder, the risks are enormous that at the end of that ten-year period there will no longer be an alternative company in existence to bid against the original bid winner. The loss of universal service funding support for a ten-year period, for example, may well have caused the incumbent to have gone out of business in the interim. The subscribers in the area at issue might then be stuck indefinitely with the provider who was unable to provide an acceptable quality of service over the first ten years.

III. Issue: Whether there are major advantages and disadvantages of using auctions for determining universal service support.

² 47 U.S.C. § 254 (b) (3).

The foregoing section highlighted several of these advantages and disadvantages. Again, the main (and perhaps the only) advantage of reverse auctions in the absence of other regulatory safeguards is that they help control the growth of the universal service fund. This is almost certainly true if there is only one winner in every qualifying service area. The "Discussion Proposal" that the Joint Board attached to its Public Notice is interesting insofar as it envisions two winners instead of one. Both winners would be required to provide voice service. One would also be required to provide broadband service and the other would also be required to provide mobility.

The Joint Board does not clarify in its Public Notice the relative importance of competition in any new reverse auction process. Under the "Discussion Proposal", the two winning bidders would likely compete to some extent with respect to the voice services they provide. For example, those subscribers who care little for either broadband or mobility might choose only one or the other of the providers based presumably on which provider they feel can deliver the best combination of factors such as price, quality of service, convenience, etc. On the other hand, as technology changes, there may be areas in which both auction winners can provide both voice and broadband services. In fact, there may even be some areas in which both auction winners can provide voice, broadband *and* mobility. Looking around Montana, we at MITS are not aware of any rural areas in

which either situation could occur today, but the situation may change significantly over the next ten to twenty years. One of the important questions in this regard is how one would define "broadband."

Presumably, that definition will evolve over time. In a number of rural areas of Montana, small rural incumbents are already building out fiber to the home and business. While we are also seeing upgrades in some wireless networks, including the gradual deployment of 700 MHz technology, the definition of broadband would still have to be pretty slow for a wireless carrier to be the broadband provider under the "Discussion Proposal."

The disadvantages of reverse auctions, as alluded to earlier, surround the meaning of the phrase "acceptable quality of service." The successful bidder will presumably be awarded some amount per line for providing an "acceptable quality of service." Perhaps the starting place for determining the meaning of "an acceptable quality of service" will start with the nine supported services established by the FCC for ETC designation. But as the FCC learned over time much of what providers and state regulators review when determining quality of service is not even addressed by the nine supported services. The nine supported services do not discuss issues such as reliability, customer service responsiveness, credit policies, truth-in-billing, etc., etc.

This whole area of "acceptable quality of service" therefore begs the question of how that phrase is to be interpreted and who is going to interpret it. Since the Universal Service Fund is a national program, one would think that there should be uniform, nation-wide standards for defining an "acceptable quality of service." On the other hand, state public utility commissions across the country determine what constitutes an "acceptable quality of service" every day for the providers they regulate. One interesting possibility is that a provider might provide an "acceptable quality of service" for the purposes of federal rules governing a particular reverse auction system of USF distribution but may not provide an "acceptable quality of service" sufficient to meet the standards of a particular state for maintaining its certificate of public convenience and necessity. The "Discussion Proposal" makes the states responsible for recommending to the FCC the choice of the winning bidders. Such a system would almost certainly result in wide disparities between the quality of service that must be demonstrated by a bidder in one state versus the quality of service that must be demonstrated by a bidder in another state.

In our view, this debate over quality of service is going to be particularly difficult when discussing mobility. For example, under current Montana rules, in order for a wireless provider to be designated as an ETC, it must show that within five years of designation it can serve

98% of the residential and business locations in the service area at issue with a service level of -104dbm or better. The -104 level was the result of negotiated compromise, and we at MITS are aware of a number of carriers that market the size of their service areas on both sides of that number.

For example, a particularly "aggressive" wireless marketer might issue its customers a map indicating that its service area consists of the area within which the signal strength is -110 or better. Many other providers would tell you that one would have to be very lucky indeed to be able to maintain a wireless connection with a signal strength that low. A more conservative marketer might define their coverage area for the purposes of their marketing materials as the area within which the signal strength is -90 or better. On the one hand, the more conservative marketer is likely to field many fewer complaints about the veracity of their marketing materials. On the other hand, that conservative definition might cause them to lose out as a reverse auction bidder based on the "perception" of those reviewing the bids that the more aggressive marketer is able to serve a broader geographical area.

Another interesting question on the wireless side concerns the affect of granting one winning bid for mobility in an area where wireless competition is still in its early stages. If, for example, there are three wireless providers serving a rural service area, each of whom has built out a few towers but none of which currently comes close to dominating the

market or serving a majority of the incumbent's study area, does awarding USF to one of the providers essentially determine which of the providers will survive? In a sparsely populated market with relatively low margins, one could certainly envision that ten years of universal service support to one of the competing carriers would quite likely drive any competitors out of the business.

On the landline side of the business, the "Discussion Proposal" raised another interesting issue during our discussions at MITS. One of the proposed provisions would allow the incumbent to elect to be the voice and broadband provider for the first ten-year period. The presence of such a provision in any reverse auction plan would be critically important in terms of garnering the support of organizations like ours that represent small, rural incumbents. However, we are aware of certain rural communities in which the local Bell company (or some other large company) had simply determined not to invest for quite some time in plant and service upgrades. In many such cases, neighboring rural telephone companies have made significant investments in competitive ventures, often taking the vast majority of the customer base from the large incumbent. Under the "Discussion Proposal," the Bell company, as the incumbent, could elect to be the broadband bidder even if it only serves 10 to 15% of the customers because of the commendable efforts of the neighboring small company to invest in a long-neglected community.

While we do not have a solution to propose at this time, something about that arrangement strikes us as fundamentally unfair.

IV. Conclusion.

We at MITS understand the political reality that unless ways are found to slow or even stop the growth of the high-cost portion of the Universal Service Fund, the program faces an uncertain political future. Some members of Congress have already apparently decided that the program has completed its mission and is no longer necessary. We would, of course, strongly disagree with this position. At the same time, we do not wish to give them even more ammunition with which to attack the program.

In our opinion, reverse auctions are unquestionably a way to reign in the growth of the high-cost portion of the Fund. However, a number of regulatory safeguards must be a part of any such program. As a matter of policy, we think that there must be a recognition that while competition is still important, a successful universal service program in the nation's most rural and sparsely populated areas may require a recognition that universal service takes precedence over unfettered competition in such areas. That seems to be the only way that a program that limits the number of ETCs that can operate in a given service areas can survive.

We also believe that any such program must exercise particular care in the area of defining quality of service. In the past, there has been too much

faith put into the notion that the market will ensure that those providing a high quality of service will survive and those providing a lower quality of service will fall victim to competition. By their very nature, financial support programs skew the way the competitive market works. If we find that the winners of reverse auctions cannot truly provide an acceptable level of quality, there is a very real danger that ten years later the providers that *were* capable of providing an acceptable level of quality will no longer be in business to pick up the pieces. Such an outcome would do a tremendous disservice to the residents of rural American and would certainly not be consistent with the lofty principles of universal service set forth in the Telecommunications Act of 1996.

RESPECTFULLY SUBMITTED This 10th day of October, 2006.

Michael C. Strand, General Counsel
Montana Independent Telecommunications Systems (MITS)